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Veröffentlichungsversion / Published Version  
Zeitschriftenartikel / journal article

#### Empfohlene Zitierung / Suggested Citation:

Romanova, T. A. (2014). Russia-EU energy efficiency cooperation in the Baltic region: the untapped potential. *Baltic Region*, 1, 21-33. <https://doi.org/10.5922/2079-8555-2014-1-2>

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# RUSSIA-EU ENERGY EFFICIENCY COOPERATION IN THE BALTIC REGION: THE UNTAPPED POTENTIAL

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*Stereotypically, the understanding of Russia-EU energy relations is often reduced to trade in oil and natural gas, which downplays the importance of energy efficiency cooperation. This cooperation is promoted within the Energy Charter and its Treaty, Partnership and Cooperation Agreement, Energy Dialogue, Common Economic Space, and Partnership for Modernisation. However, it lacks practical development, which relates to the instable legal environment in Russia, insufficient mechanisms of financial support for energy conservation projects and poor political support. Nevertheless, energy efficiency cooperation is capable of changing Russia-EU energy cooperation qualitatively: it offers a cheaper way to meet the needs of the EU, redefines interdependence between the parties and introduces new elements of equality between them. Energy efficiency cooperation also transforms the patterns of the Russia-EU legal harmonization, creates new conditions for the convergence of regulations and the development of the middle class in Russia. Due to its specific features, cooperation in the Baltic Sea region can become a locomotive of the Russia-EU energy efficiency cooperation, and, as a result, strengthen relations between the partners.*

**Key words:** Russia-EU relations, energy, energy efficiency, normative power, legal convergence

The stereotypical idea of Russia-EU energy relations usually boils down to trade in hydrocarbons. The range of widely discussed issues includes the Third Energy Package and its impact on Gazprom, the construction of the Nord and South Streams for exporting Russian gas to the EU, the attempts to secure a bypass route for transporting resources from Central Asia, and export duties on Russian oil and oil products. These issues of considerable geo-

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*Submitted on December 15, 2013*

doi: 10.5922/2079-8555-2014-1-2

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political and economic significance overshadow cooperation in increasing energy efficiency. However, the latter is an element of Russia-EU cooperation beyond the field of energy.

Let us focus on Russia-EU relations in the field of energy efficiency. At first, we will demonstrate the significance of energy efficiency for Russia and the European Union and then address the corresponding forms of cooperation. We will also show that joint projects in the field of energy efficiency transform energy relations and have potential for enhancing international cooperation on the whole. Finally, we will consider the role that the Baltic region can play in energy efficiency cooperation.

### **Energy efficiency in the policy of Russia and the EU**

Both Russia and the European Union pay significant attention to the problems of energy efficiency. It is regularly considered in a triad with reducing greenhouse emissions and developing renewable energy sources (RES).

In Russia, framework documents on energy industry development, which have been produced since the early 1990s, pay attention to this problem. According to some calculations, Russia's untapped energy efficiency potential is comparable to the annual energy consumption in France [1]. Energy efficiency became a real priority in Russia only after a corresponding presidential decree was signed on June 4, 2008 [2]. It was the first document to set the target of reducing the power intensity of Russia by 40% until 2020 in comparison to 2007.

During the revision of Russia's energy strategy in 2009 and its prolongation until 2030, energy efficiency was named one of the key priorities of the state's long-term energy policy [3]. Moreover, the methods of developing the 40% energy saving potential were described in detail. A federal law on energy saving was approved [4], and, later, a state action programme was developed [5].

In 2009, Russia's energy efficiency assumed political significance: leadership in the field of efficiency of production, transportation and energy use was mentioned among the five strategic vectors of modernisation [6; 7]. (However, energy efficiency did not retain its significance within the concept of new industrialisation promoted by V. Putin.)

In the European Union, energy efficiency legislation was developing simultaneously with the processes described above. The first documents setting energy reduction targets were drawn up in the 1990s [8], though the idea of energy efficiency has been promoted in the Old World since the energy crises of the 1970s. However, an increase in energy efficiency became a political priority in the 21<sup>st</sup> century, when the European Commission set out to prepare a specified action plan [9] as well as the Green Paper on Energy Efficiency [10]. The latter document sets the target of reducing energy consumption in the EU by 20% by 2020. The EU aligned these targets with Kyoto commitments relating to the reduction of greenhouse emissions.

In 2007, the European Commission and the EU member states revisited the issue of energy saving commitments and energy consumption reduction. In 2007, the European Council confirmed the EU's 20% commitment, which became part of the so-called 20—20—20 strategy (20% reduction of greenhouse emissions, 20% increase in energy efficiency, 20% increase in RES in the energy mix) until 2020. It is of interest that the Commission did not manage to convince the member states to approve legally binding targets in energy efficiency (which was the case in greenhouse emissions and increasing RES percentage). The 2011 plan to increase energy efficiency [12] was non-regulatory. Only individual mechanisms (commitments of power supply companies and authorities) were mentioned in the 2012 energy efficiency directive [13].

It is worth noting that, both for Russia and the EU, an increase in energy efficiency is an immediate priority. However, in the triad of “energy efficiency — greenhouse emission reduction — RES development”, the first component is of crucial significance for Russia, whereas the EU focuses on the other two. It is explained by a number of circumstances. RES development is hampered in Russia by traditional energy sources and a lack of interest from large companies in investing in non-traditional energy. In the EU, a prevalent opinion is that renewable energy sources contribute to the Union's energy efficiency through replacing imported hydrocarbons. A reduction in greenhouse gas emissions is the core of the regulatory power of the EU (i. e. the values it strives to protect) and is one of the principles of its conduct in the international arena. In Russia, reducing greenhouse gas emissions is perceived as an expensive image ‘campaign’ that can decelerate the country's economic growth.

Despite these differences, the EU and Russia have actively developed cooperation in energy efficiency. Its key element is technology transfer from the EU to Russia (through exporting corresponding goods and services). The institutional mechanisms of these interactions are discussed in the section below.

### **Forms of Russia-EU cooperation in the field of energy efficiency**

Russia-EU energy cooperation began with the 1991 Energy Charter and the Energy Charter Treaty (ECT, 1994). The latter even included a special protocol on energy efficiency [14]. Alongside trade, transit and investment, energy efficiency became one of the pillars of the ECT. Moreover, it was one of the most noncontroversial issues in this dialogue. Throughout the history of the Energy Charter Secretariat, the energy efficiency of many ECT members was analysed, which helped to identify the potential for further cooperation, and knowledge and technology exchange. However, the ECT was not implemented to its full potential in Russia-EU relations. Russia kept postponing its ratification and finally abandoned the idea. The EU participation was undermined by arguments over the distribution of competences between the Union and member states, and the increasing gap between the ECT provisions and domestic market regulations.

The Partnership and Cooperation Agreement between Russia and the European Union (PCA) [15] had little effect on the quality of relations between the partners in the field of energy. The key reason behind it was that the ECT and the PCA were developed simultaneously. Therefore, a decision was reached to avoid the duplication of provisions through including into the PCA references stating that the key parameters of Russia-EU energy cooperation were regulated by the ECT. These references can be found in Articles 65 and 105 of the Agreement. Energy efficiency and energy saving were also mentioned in Article 65 as a priority area of cooperation. Thus, the document emphasised their significance and the partners' mutual interest in a dialogue focusing on these issues. However, the non-ratification of the ECT by Russia *de facto* brought further development of cooperation to a standstill.

Another important tool of Russia-EU cooperation in the field of energy is the Energy Dialogue. In the final reports of the Russia-EU summit of October 30, 2000, which initiated the Dialogue, energy saving was named as one of the key aspects of cooperation [16]. The transfer of European experience and developments was emphasised more strongly than before. The energy dialogue was never meant to replace legal provision. It was positioned as an exchange of ideas between public officials and businesspersons aimed at improving the conditions of practical cooperation and mutual socialisation [17].

In February 2006, Russia and the EU launched an energy efficiency initiative in the framework of the Dialogue. Three regional pilot projects aimed at the transfer of practices and technology from the EU to Russia were implemented in Arkhangelsk, Astrakhan and Kaliningrad in 2006—2007. Each of the three centres focused on increasing energy efficiency in a certain field (energy supply in Astrakhan, industrial consumption in Kaliningrad and utility consumption in Arkhangelsk). In 2007, in the framework of the Dialogue, permanent intergovernmental institutions were established. They involved mid- and lower-level officials in the process (the so called thematic groups). One of the institutions was meant to focus solely on the issues of energy efficiency. It emphasised the significance of energy efficiency and the mutual interest of the parties. Despite the ensuing restricting of the Dialogue institutions, the energy efficiency group was not dissolved [17]. Finally, the interaction in the framework of energy efficiency was acknowledged by the parties as one of the achievements of the decade-long Dialogue in 2011 [18].

So far, the greatest accomplishment of the Energy Dialogue is the Roadmap of the EU-Russia Energy Cooperation until 2050 [19]. This document puts cooperation in energy efficiency on a par with the dialogue on oil, natural gas and electricity. Moreover, according to the Roadmap, “cooperation potential is immense and could both in the short and long term contribute to the objective of a Pan-European energy area” [19, p. 29]. The document also calls for regular exchange of information on the concepts and institutions of their implementation, commercial conditions and technologies. At the same time, “energy efficiency without borders” was named as the long-term objective [19, p. 30], whereas interim objectives are given clear descriptions and timelines.

Cooperation in the field of energy efficiency was also part of Russia-EU projects of general nature. Firstly, it was integrated into the economic cooperation; the corresponding roadmap was developed in 2005 [20]. Thus, energy efficiency projects were given an opportunity to apply for governmental financial support, which was implemented within the common energy efficiency space instrument (launched in 2010). Moreover, the integration of the Energy Dialogue into the Common Economic Space made it possible to disseminate positive experience of energy cooperation (including a dialogue of stakeholders from the private and public sectors) within other branches of economy.

Secondly, increasing energy efficiency became one of the pillars of the Russia-EU partnership for modernisation. This course of events was rather logical, since this initiative followed the logic of the modernisation process in Russia [21]. The partnership contributed to a more accurate description of parameters of interaction in the field of energy efficiency — namely, support for pilot projects, advanced training for Russian specialists and energy saving awareness development among Russian citizens. Moreover, special financial projects were launched by two Russia's major banks, Sberbank and VTB, to support Russia-EU cooperation in the field of energy efficiency.

Finally, the last form of Russia-EU cooperation in energy efficiency is bilateral agreements between Russia and some individual EU member states (the Netherlands, Germany, Finland, Ireland, France and Greece). The best known example of such cooperation — mostly due to the scope of its activities and involvement in the modernisation process — is the Russian-German Energy Agency established in 2009.

Thus, over many years, Russia-EU cooperation in the field of energy efficiency has been developing in several parallel and mutually supportive forms. However, the achieved results are still modest: technology transfer has been faced with certain problems, and the number of joint projects — especially those in the Russian regions bordering on the EU — is rather limited. One of the most commonly mentioned reasons behind it [22] is an insufficiently favourable investment climate in Russia, which is partially a result of lacking clearly defined legal conditions. Another obstacle is limited financial incentives for companies operating in the field of energy efficiency. Of course, clearly defined legal conditions and predictability of political leadership's actions are more important in this field compared to oil and gas trade, where an alliance of giant corporations and the political leadership of countries or the EU can remove any obstacles.

One of the reasons behind modest achievements of cooperation in energy efficiency is a lack of political attention, which — as paradoxical as it sounds — results in negative depoliticisation. Since cooperation in this field does not attract the attention of the political leadership, it is supported — both politically and legally — on the “leftover” principle. Energy efficiency is brought into focus when there is a need to show mass media that Russia and the EU have accumulated a large body of positive experiences. However, this approach underestimates the potential of energy efficiency in the field of energy and Russia-EU relations in general. This aspect will be discussed in the section below.

## Energy efficiency as a catalyst to transform Russia-EU relations

In our opinion, there are at least three aspects that make it possible to speak of cooperation in energy efficiency as a catalyst for transforming Russia-EU cooperation in the field of energy.

Firstly, as it was mentioned above, the energy saving potential is immense in Russia. According to official documents, Russia consumes 40% more energy than it could. Russia's geographical conditions are such that the main resources are deposited in the east (new deposits are increasingly found closer to the Pacific and Arctic Oceans, farther from the developed infrastructure). At the same time, the key consumption areas, according to the established industrial and population distribution patterns, are situated in the European part of the country, i.e. in the immediate vicinity of the European Union.

Today, Russia-EU relations in the field of oil and natural gas supply are experiencing a difficult stage. The EU strives to reduce its dependence on oil and natural gas from Russia. This trend is being reinforced by the new member states, especially Poland and the three Baltic states. There is growing discontent with the European market in Russia, which is focused on the Third Energy Package aimed at complete liberalisation of natural gas and electric power markets. Since the EU is Russia's principal export market, the eastern partner (represented by Gazprom) becomes a "prisoner" of decisions made in Brussels. These decisions transform the field of Russia's economic activities, and Moscow is unable to affect the situation. It creates a phenomenon that has been called "a diversification race" [23]. The EU strives to reduce its dependence on hydrocarbon supply from Russia, whereas the latter sets out to develop different export markets (Asia). In this context of mutual distrust, one can hardly expect that pipelines will run from new Eastern Siberian deposits or Russian Asian Frigid Zone to the European Union.

At the same time, the gradual depletion of old fields, the pressure of the current obligations to the New World (especially, those within long-term contracts) and the increasing demand for hydrocarbons in the EU raise the question of a new strategy on the European market. It would be optimal to increase energy efficiency in the European part of Russia and to export the surplus to the European Union. In the current condition, such a strategy of supporting exports to the EU seems to be the most economically feasible in comparison to transporting hydrocarbons from the distanced (eastern) regions of the country. Another favourable factor is the concentration of power consumption in the large cities of the European part of Russia that have a connection to the pipeline systems running to the EU and can provide significant amounts of natural gas to be saved.

Another aspect that makes it possible to speak of energy efficiency as a catalyst for energy relations transformation is technology. Traditionally, those EU representatives who exhibit anti-Russian sentiments speak of asymmetric dependence on Russian energy. In fact, one should speak of interdependence: the EU needs energy, and Russia needs oil and gas revenues. However, this dependence is manifested in different ways: in a short-term

perspective, irregularities in resource supply will, to a greater degree, affect the EU as it will face problems with meeting industrial and utility needs. Irregularities in payments are less evident in a short-term perspective. At the same time, in a long-term strategic outlook, Russia's dependence on a situation on its principal export market and the EU regulations becomes evident.

An entirely new situation arises in case of an increase in energy efficiency based on EU technology. Potentially, Russia may experience technological dependence from the EU, which will be most pronounced in a short-term perspective (especially, against the background of a need for new specialists, spare parts, etc.). However, in a long-term perspective, countries of Russia's potential can organise independent production of necessary goods and services based on the use of EU technology. The EU will be faced with a different situation: its dependence on Russia's large export market will develop in a long-term prospective.

In other words, within cooperation in energy efficiency increase, the balance of forces is in inverse proportion to that characteristic of hydrocarbon trade. Russian companies become susceptible in a short-term perspective with an opportunity of long-term emancipation from EU producers; the latter experience long-term dependence on the export market. As a result, cooperation in energy efficiency can become a counterweight to oil and gas trade. Thus, equality can be achieved between Russia and the EU. It will have a favourable effect on the Baltic Sea region, where many countries depend on Russian resources and tend to politicise this dependence as a result of their historical experience.

Finally, the third aspect of energy efficiency increase as a catalyst for the transformation of Russia-EU cooperation is potential changes in the process of legal harmonisation.

Since the signing of the PCA, the approximation of Russian and EU legislation (Article 55) was based on the fact that the EU strongly insisted on the assimilation of Russian regulations to those existing on its territory. The disadvantages of this approach are evident. Firstly, it contradicts the basic principle of Russian foreign policy — Moscow's equality with the key global players. Secondly, the solutions developed by the EU through an uneasy compromise reached by the member states are not optimal and beneficial for Russia, which is often faced with other problems. Moreover, a conflict-fraught nature of unilateral legal harmonisation is also characteristic of the Third Energy Package, within which the EU imposes its decisions on Moscow. In this way, the EU tries to ensure competitiveness on its natural gas market (also by means of eliminating Gazprom's export monopoly and further market liberalisation in Russia).

Energy efficiency is a rather curious case in terms of legal harmonisation. It is an area where the interests of Russia and the EU coincide. Furthermore, it is an area where both partners make synchronous steps towards the same goal, and they often use the same instruments (transition to more efficient household appliances, energy labelling, etc.). In other words, it is a situation of joint development and testing of new measures to reach a common goal rather than simple adoption of the EU practices by Russia. It cre-



ates a basis for ensuring qualitative equality between Russia and the EU. In view of that, energy efficiency is largely a responsibility of small and medium enterprises and hardly depends on geopolitical considerations. This method of ensuring equality in legal harmonisation creates a solid basis for positive depoliticisation of cooperation.

The prerequisites for equality and depoliticisation emerging in energy efficiency cooperation are of importance for the entire range of Russia-EU energy relations.

### **Energy efficiency in a broad context of Russia-EU relations**

Russia-EU cooperation in the field of energy efficiency has an immediate effect on the whole pattern of interconnections. It is not only a result of the fact that, as the Roadmap stresses, “energy efficiency objectives have a strong impact on other policy areas, notably in transport sector and urban planning” [19, p. 28]. It is a result of transformations in the energy industry. However, we would focus on its strategic aspects.

Firstly, one cannot but notice that the positive experience of legal harmonisation is important not only for hydrocarbon trade but for the system of Russia-EU relations on the whole. In a situation when the partners pronounced the development of a free trade zone as one of cooperation objectives and the EU accounts for almost a half of Russian imports, legal approximation is inevitable in most economic areas. The question is whether the partners will be able to focus on the technical aspect, and to leave the work to experts, lower-level officials and businesspeople. The problem is that, with each step up the administrative and hierarchical ladder, a desire to look for a mutually beneficial solution decreases, whereas politicisation of the issue (i. e. its consideration in the context of package deals) increases.

In this case, the experience of cooperation in energy efficiency, where the partners have managed to set similar targets and reach them in the framework of a dialogue, could serve as a good example. In other words, there is a need to revisit the positive experience of legal harmonisation in this field and to consider the opportunities for its multiplication in other areas.

Secondly, cooperation in the field of energy efficiency involves predominantly small and medium enterprises. This has at least two implications:

1. For small and medium enterprises, legal approximation is more important than for giant concerns. They also need a stable legal climate. Unlike their “elder brothers”, small and medium enterprises cannot afford to employ a department of lawyers, managers and lobbyists, nor can they build a close alliance with the government. Hence, in the presence of political will, cooperation in the field of energy efficiency should contribute to legal harmonisation and the improvement of investment climate in Russia and, therefore, legal predictability.

2. In most developed countries, small and medium companies are main employers. Therefore, an increase in the number of Russia-EU projects in the field of energy efficiency should contribute to a change in the pattern of

employment and the development of the middle class in Russia, which is traditionally interested in a stable legal environment and a high level of political culture.

Finally, cooperation in the field of energy efficiency facilitates legal approximation between Russia and the EU. In EU-Russia studies, there is a “tradition” to speak of a conflict between Russia’s interests and the EU’s values, and their incompatibility, as well as the need for the partners to understand each other. In effect, interests can hardly exist without values and vice versa. Interests are always a product of value. In one case, they can be pragmatic and, in other case, they are more idealistic and non-material — at least, when expressed on paper.

For example, let us consider the Russia-EU modernisation dialogue. Russia emphasised the priority of economic modernisation over the political one, since there is a need for a solid technological and economic basis that would contribute to the strengthening of democracy and the rule of law. The European Union insisted on the precedence of political reforms, development of human rights, democracy and the rule of law to create an environment for new industrialisation and ensure the modernisation of the economic environment [24]. It is a result of differences in patterns rather than in values and regulations.

Is there convergence between them? We believe that convergence exists. Energy efficiency is a good example thereof. Russia-EU cooperation in energy efficiency is a case of practical interaction. Its characteristics are determined by different patterns. Russia gives priority to the economic and technological considerations, and commitments to viable solutions. For the EU, increase in energy efficiency is connected not only with pragmatic reasons (however, they were the starting point of energy efficiency development in the Old World in the 1970s), but also with environmental needs and concerns — an integral part of the EU pattern. Of course, each party has its own logic. However, the key element is their interaction and mutual socialisation. In the case of energy efficiency, this socialisation is of special interest, since it involves almost all levels of authorities and society — from governmental structures of the federal and regional levels to small businesses. This multi-level socialisation makes it possible for the partners to know each other better, which creates opportunities for gradual convergence of values.

However, these are not opposite ideas but rather different facets of the same process. Both pragmatism and technical thinking have been characteristic of Europeans. Their experience in the field of energy efficiency (including the fact that they are reluctant to set legally binding targets) is a proof thereof. Thus, approximation of values is possible, the more so in such politically insignificant areas as energy efficiency.

Finally, there is another factor contributing to the value convergence between Russia and the EU: energy efficiency requires advanced training and thus engages citizens. The activity of citizens is a bottom-up phenomenon. Therefore, the energy efficiency dialogue should contribute to the strengthening of civil society, which will also have a favourable effect beyond the field of energy.

Consistent work on energy efficiency as an area of cooperation and due attention of the political leadership (i. e. positive politicisation) will facilitate the elimination of barriers to cooperation — first of all, the lack of predictability of legal climate in Russia. At the same time, the changes should take place gradually through a bottom-up initiative, which will make them more solid than mere talks about the need to ensure the rule of law.

### **The Baltic region in Russia-EU energy cooperation**

As mentioned above, the ramifications of energy efficiency cooperation go far beyond its area. It has potential to transform the whole system of Russia-EU energy relations through changing the quality of their interdependence, introducing elements of equality, and offering a cheaper and simpler method of meeting the increasing needs of the EU. Energy efficiency also has a positive effect on legal harmonisation, regulatory approximation, and the creation of a stable middle class — the pillar of democracy and a legal state.

Let us consider the role of the Baltic region in Russia-EU cooperation in energy efficiency.

Several years ago, a widely discussed topic was the creation of an energy partnership in the framework of the Northern Dimension, which was meant to supplement the two existing ones focusing on environmental issues, and public health and social well-being. As a result, partnerships on transport and logistics, and culture emerged. As to energy, it was decided that hydrocarbon trade was the realm of high politics, whereas the existing Northern Dimension Environmental Partnership covered the RES development and energy efficiency. In fact, as it was mentioned above, energy efficiency (as well as RES development) can transform both energy cooperation and the whole system of Russia-EU relations.

There are several prerequisites for an active participation of the Baltic region in this process. Firstly, the Baltic region is the site of the most prolific contacts between Russia and the EU. The immediate geographical vicinity facilitates these contacts. Moreover, the cooperation experience accumulated since the 1990s and the density of contacts make the region special in many areas including energy efficiency. Over the years, the parties have learnt to listen to each other, which often ensures success.

Secondly, the Nordic countries have achieved considerable results in energy efficiency. Their accomplishments have become a benchmark for the current energy strategy of Russia [3] in terms of the need to reduce energy consumption to a level comparable to that of the developed countries situated in similar climatic conditions.

Thirdly, the Nordic countries have outstripped their EU colleagues in taking energy efficiency beyond the areas of pure pragmatism. In this context, of special importance are environmental values, as well as civil initiatives, the ability to listen to society and the support of bottom-up projects. Mutual socialisation of Russia and the Nordic countries is a more radical instance of legal approximation.

Fourthly, it is not a secret that cooperation in the Baltic region is highly institutionalised. The Baltic institutions include the Northern Dimension (which comprises the above mentioned Environmental Partnership), the more formalised Council of Baltic Sea States, and the industry-specific Baltic Sea Region Energy Cooperation (BASREC) and the Dialogue Platform on Energy and Resource Efficiency in the Baltic Sea. Finally, Germany, Denmark, Finland and Norway, a non-EU state, are implementing projects on energy efficiency and RES development in collaboration with Russia (predominantly, in the northwest of the country).

Finally, unlike other EU regions, cooperation between the Baltic countries is also targeted at the needs of small and medium businesses. There are different instruments for financing smaller projects (for example, the Nordic Investment Bank), which serve as the basis for cooperation in energy efficiency.

Therefore, Baltic cooperation in energy efficiency has potential for further development. It can also facilitate a qualitative change in Russia-EU energy relations and cooperation in general. Regional interactions are optimal for forging stable Russia-EU relations based on mutual trust, and gradual convergence of legislation and basic regulations. It can be achieved through implementing certain projects that will lay the foundations for further conceptual changes.

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